Foreword

In modern states, the joint work of a number of institutions helps to ensure that the welfare of a given community or society is enhanced. Economic policy actors are characterised by both unity and diversity, because – while they share a common purpose – these actors, by their very nature, all have different mandates and different ways and means of achieving common social goals. In this complex system of goals and instruments, independent central banks played and play a particularly important historical role, having been created with the specific aim of supporting the emergence and sustainability of well-being and prosperity by ensuring the stability of money, the financial system and the economy as a whole.

In Hungary, this role of preserving stability is played by the Magyar Nemzeti Bank (the central bank of Hungary, MNB), which celebrated its centenary in 2024. This issue of the Financial and Economic Review pays tribute to this landmark anniversary with articles by renowned and respected international and domestic experts, pointing out that the values of predictability, resilience and safety are common and solid foundations across time and borders, upon which central banks' activities are based all around the world. This is in line with our belief that a central bank can do the most for long-term economic growth and thus social welfare if its decisions are guided by these values, providing a stable basis for the functioning of the economic and financial system.

The festive character of our December issue is reinforced by the opening essay by *György Matolcsy*, Governor of the Magyar Nemzeti Bank. His article is a centenary reflection on the mission of the MNB, and his analysis aims to draw on historical lessons to provide a guide to the challenges of our day and age. What emerges from the historical periods is the important requirement to preserve the independence of the central bank and to coordinate the activities of the different economic policy branches, in order to achieve and maintain price and financial stability, to support economic development and to prepare for the challenges of the future, such as the green transition.

Barry Eichengreen, Professor at the University of California, Berkeley, and Researcher at National Bureau of Economic Research and Centre for Economic Policy Research, also analyses the relationship between central bank independence and monetary stability. His essay compares monetary policy and inflation in Hungary in the first half of the 1920s and the first half of the 1990s, when economic and financial imbalances put the central bank under inflationary financing pressure. According to the author, central bank independence has proven useful, but in neither case has it been sufficient to prevent the instability that later developed in a situation where the central bank was under the pressure of expectations to resolve problems emanating from the banking sector, the balance of payments, the budget and weakened sectors of the economy.

Harold James, Professor at Princeton University, describes the period of hyperinflation in Central Europe after the First World War, with a special focus on Germany and Poland. He points out that the peripheral countries concerned also sought to use inflation to change international and internal redistribution, so that the elimination of inflation was accompanied by the surrender of some aspect of sovereignty or the restriction of domestic policy space. As a result, many of the inflationary processes did not actually end, with premature, incautious celebrations followed by worsening inflation.

Manoj Pradhan, founder of Talking Heads Macro, and *Charles Goodhart*, Emeritus Professor at the London School of Economics, jointly discuss the correlations between demographic change, budgetary risks and monetary policy. The researchers start from the premise that there are indications that the size and persistence of future deficits and debts are being underestimated, and conclude that we are entering a new era in which the relationship between demography and fiscal and monetary policy will become even more complex than it is today.

One of the key issues still roiling the world of central banking today is discussed in the joint paper by *Paul De Grauwe*, Professor at the London School of Economics, and *Yuemei Ji*, Professor at University College London, who explore how to fight inflation without central banks providing substantial transfers to banks. On this issue, the authors propose that central banks should introduce a two-tier system for the establishment of minimum reserves, in which interest would only be paid on the amount above the minimum reserve. This would dramatically reduce allocations to banks, allow central banks to maintain the current procedure and render monetary policy more effective in the fight against inflation.

The study by *Reiner Martin*, Executive Director at the National Bank of Slovakia, and *Piroska Nagy Mohácsi*, Visiting Professor at the London School of Economics, examines the post-pandemic inflation wave through the example of the Visegrad Group (Visegrad Four) countries. They find that membership of the euro area was not only beneficial in normal economic circumstances, as the advantages of monetary sovereignty in small, open and integrated economies gradually disappeared, but was also particularly useful in times of crisis.

György Szapáry, Chief Adviser to the Governor of the MNB and Visiting Lecturer at the Budapest Metropolitan University, and *Balázs Vonnák*, Economic Adviser at the MNB and Visiting Lecturer at the Budapest Metropolitan University, examine the impact on convergence of the decisions of monetary policy institutions in Central and Eastern European countries. Their main finding is that the convergence rate over the past decades has depended only to a small extent on the choice of the exchange rate regime or the potential adoption of the euro or inflation targeting, but much more on the establishment of central bank independence. This suggests that central bank independence significantly enhances the credibility and predictability of monetary policy and largely determines the success of each monetary regime.

István Ábel, Professor at Budapest Business University, and *Pierre L. Siklos*, Professor at Wilfrid Laurier University and Balsillie School of International Affairs, use a theoretical model in their study to assess the main elements that determine the monetary policy strategy chosen by central banks to control inflation, especially in their flexible inflation targeting regime, in which exchange rate developments play a significant role. Empirical evidence from Taylor's rules suggests that the MNB is pursuing a flexible monetary policy that contributes to the stabilisation of the economy.

The theoretical model put forward by De Grauwe and Ji is complemented by a study by *Csaba Csávás*, *Pál Péter Kolozsi* and *Ádám Banai*, Experts at the MNB, which examines the modification of the Hungarian minimum reserve system between 2022 and 2024 as a case study and concludes that there are substantial and strong constraints on the reduction of interest payments on the minimum reserve: for a given overall interest rate level, it may reduce central bank interest expenditure, but the extent of the reduction is limited by the potential consequences of the change for the overall money market environment and foreign exchange supply as an unintended cost.

The topic of the feature article in this issue looks clearly to the future. *Bin Hu*, Associate Professor and Director of Global Climate Governance Research at Tsinghua University, *Chaoyi Chen*, an Expert at the MNB and Visiting Lecturer at Budapest Metropolitan University, and *Yueran Zhang*, a Student at Renmin University of China, review past China-Hungary green bond cooperation and make suggestions for improving future cooperation. Key proposals include better communication and coordination in managing financial risks, opening the green bond market in both directions, establishing mutual recognition mechanisms for green bond standards and improving transparency.

The Financial and Economic Review has always made it a priority to contribute to Hungary's advancement by facilitating an understanding of the ever-changing economic developments and analysing the country's economic and financial situation. This issue once again serves that objective, featuring articles by exceptionally distinguished authors. The studies published and the historical experience they draw on clearly show that, while stability is often taken for granted, it is something that both independent central banks and economic policy as a whole must consciously work to achieve and maintain.

The best way to prepare for a leap in the economy, as in sports, is to have both feet on the ground beforehand. On this note, I offer you the studies of our jubilee issue and wish you pleasant, informative reading!

Barnabás Virág
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